1 August 2025

The cloud lifts on tariffs

- **Tariff threats and trade deals were a key theme in July; tail risk of a global trade war evaporated as countries capitulated to Trump's demands; more certainty provided on where the US is landing on tariffs**
- **Risk appetite higher, but closing of short positions in the USD drove broad gains, following its slump in the first half of 2025**
- **NZD/USD down 3½%, with mainly small net changes on the crosses**

	Quick Outlook	July Ranges
NZD/USD	Pullback in July reduces the hurdle for upward trend to reemerge after the positioning shakeout in the USD ends. We'll need to see some weaker US data and Fed rate cuts later in the year to achieve our year-end target of 0.65.	0.5890 – 0.6120
NZD/AUD	The cross is expected to continue to track directionless over the foreseeable future, with the outlook for the NZ and Australian economies similar at this juncture, following a prolonged period of NZ economic underperformance.	0.9100 – 0.9290
NZD/GBP	NZ and UK economies are both struggling; NZ-UK rate spreads should lift. Hard to get bearish on the cross rate at current levels. We have a modest positive bias over the year ahead.	0.4400 – 0.4490
NZD/EUR	Europe should be a key benefactor of any asset allocation out of US assets, and this should be euro-supportive, alongside easier fiscal policy, led by Germany. But from current low levels in the cross rate, we have a small positive bias for trading over the second half of 2025.	0.5080 – 0.5190
NZD/JPY	Continues to defy gravity, with recent tariff uncertainty and the election providing cover for the BoJ to leave policy unchanged, despite high inflation. Clear path ahead for lower NZ-JP rate differentials which should pave the way for a weaker cross-rate in time.	87.0 – 89.1

Risk appetite was higher in July, supported by reduced uncertainty about the outlook, with more clarity on where Trump was settling in terms of import tariffs. Many countries capitulated to Trump's demands and agreed to higher tariffs to avoid even more punishing tariff rates. The passing of a massive reconciliation bill in the US also provided more clarity on the US fiscal outlook. Global equity markets rose to fresh record highs. After reaching a fresh 2025 high early in the month, NZD/USD closed down 3½%, against a backdrop of a broad recovery in the USD.

Trump's tariff agenda dominated headlines through the month, with a scramble for the US to do trade deals with countries ahead of the 9-July deadline, later extended to 1-August. For some countries, Trump posted letters indicating new tariff rates that would apply from 1-August and for many these were close to the punitive rates announced on Liberation Day, between 20-30%.

Notable trade deals with Japan and the EU were agreed, both seeing a 15% tariff rate that would also apply to autos and both agreeing to significantly increase investment in the US. Vietnam would face a 20% tariff, rising to 40% for goods transhipped through the country, aimed at hitting Chinese goods that are re-exported from Vietnam. Trump threatened to lift tariffs on Canada to 35% and Mexico to 30% for goods that were not compliant with the USMCA. Trump announced a 50% tariff for Brazil, more a political decision directed towards punishing Brazil's current government than a metric related to trade imbalances. Trump said he planned to set tariffs "in the range of 15-20% "for essentially the rest of the world", referring to those countries that don't strike a deal before the 1-August deadline.

Trump planned to implement a 50% tariff rate on copper as part of a set of looming sectoral tariffs (separate to the country level tariffs). There was a backtrack at the end of the month, with the revelation that the tariff would only apply to semi-finished copper products. On pharmaceuticals, he said higher tariffs wouldn't come in for another 12-18 months, but they're going to be tariffed at a very high rate 200%. Trump also threatened to impose an additional 10% tariff on any country aligning themselves with "the Anti-American policies of BRICS".

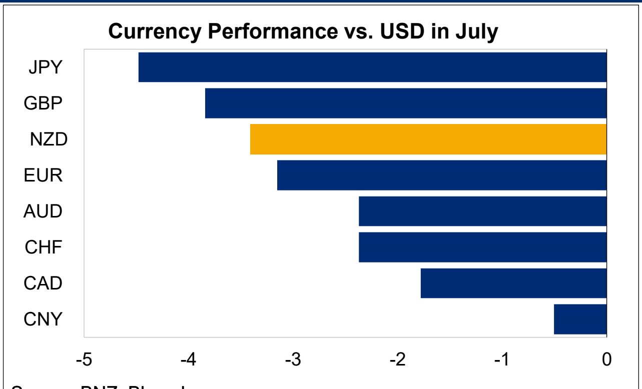
Yale's Budget Lab estimated that the average effective US tariff rate would rise to a 90-year high of 18.4%, incorporating all the latest announcements. The impact would reduce US GDP growth by 0.5 percentage points over 2025 and 2026.

Market reaction to tariff headlines was subdued, compared to the extreme volatility seen in the first half of April, a sign that investors have accepted the fact that US tariffs would lift to a historically high rate, but not enough to significantly derail global growth. In fact, the announcements provided more certainty about the economic outlook and significantly reduced the tail-risk of a major global trade war, with countries resigned to accepting US demands without retaliation.

Furthermore, reduced US-China trade tensions were evident, with no further increase in tariffs on China appearing imminent, ahead of potential for a meeting between presidents Trump and Xi later in the year.

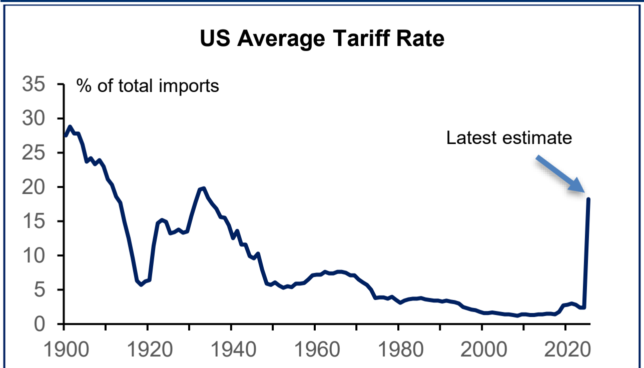
Risk appetite improved during the month, boosted by US trade deals. BNZ's risk appetite index rose to as high as 75%, its highest level since February, supported by a VIX index that fell below 15 and further compression in high yield credit spreads, which fell into the 97th percentile in terms of stretching to historical lows.

Key majors weaker against the USD in July



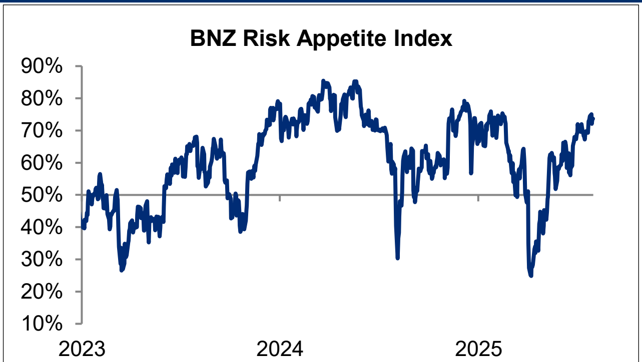
Source: BNZ, Bloomberg

US average tariff rate jumps to 90-year high



Source: BNZ, US Tax Foundation, Yale Budget Lab

Risk appetite recovers to five-month high



Source: BNZ, Bloomberg

Trump signed his One Big Beautiful Bill Act into law, which contained tax and spending policies that formed the core of his second-term agenda. The Act made permanent the cuts to individual tax rates that were made in 2017, added further tax relief, and made significant cuts to Medicaid spending to help offset the fiscal impulse. The Congressional Budget Office estimated that the Act would add $3.4 trillion to budget deficits over the next 10 years. From a market perspective, the Act provided more clarity on the fiscal outlook and raised the debt ceiling, extinguishing short-term tail default risk.

US data released during the month, were weighted more towards positive than negative surprises. GDP rose at an annualised 3.0% in Q2 following the 0.5% fall in Q1, with volatility driven by imports surging and then slumping, as businesses front-loaded imports ahead of higher tariffs earlier in the year. Domestic demand growth was sluggish in the first half, stepping down from rates seen during 2024. Employment growth remained solid, and the unemployment rate ticked down to 4.1% in June. US inflation data provided further evidence that increased tariffs were feeding through into higher goods inflation, although it was still early in the process, while softer domestic demand was contributing to weaker services inflation.

The US Fed kept policy on hold. The defining feature of the meeting was two dissents in favour of a rate cut by Trump-appointees Waller and Bowman. While this was widely anticipated, it was the first occasion of more than one Governor dissenting since 1993 (dissents by regional Fed Presidents are more common). While there was some chance of Chair Powell opening the door to a September rate cut, in his press conference he played with a straight bat, saying “we have made no decisions about September”.

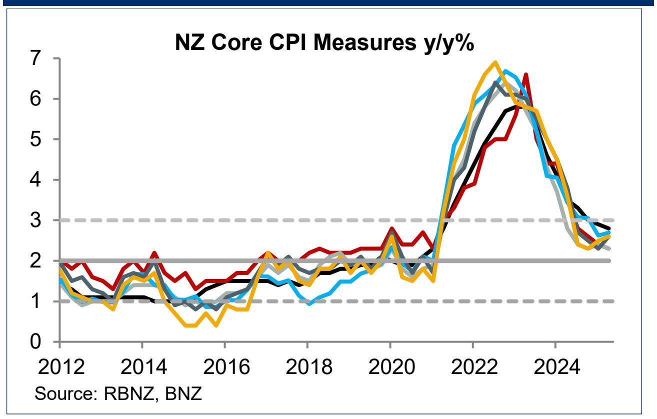
At month end, the market had priced in 33bps of Fed rate cuts through the remainder of year, compared to 67bps priced at the start of the month. While the well-established trading ranges for Treasuries continued, the curve flattened for the month, with the 2-year rate up 24bps to 3.96% and the 10-year rate up 15bps to 4.38%.

Turning to NZ, the RBNZ left the OCR unchanged at 3.25%, the first pause in the easing cycle since it began in August last year. The minutes revealed some robust debate on whether to cut again or hold policy steady, with a consensus to hold. The door was opened to a rate cut in August, with an explicit easing bias reintroduced into the press release.

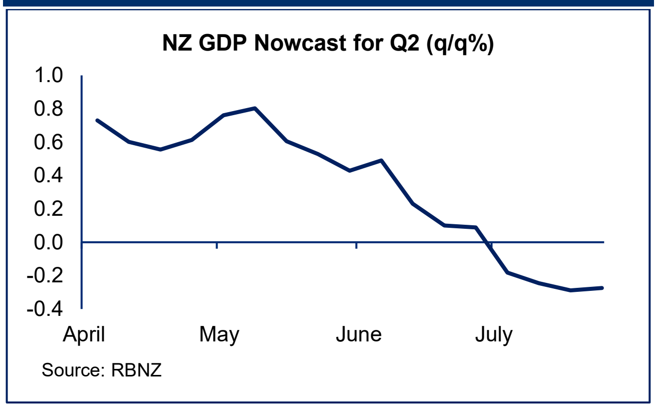
Inflation data were at the softer end of expectations, with the CPI rising 0.5% q/q, pushing up the annual increase to 2.7%. Core measures were mixed, ranging from 2.3-2.8%. The market saw the lift in inflation as temporary, and not getting in the way of a likely 25bps rate cut by the RBNZ in August. Activity data continued to point to a sluggish economy, consistent with a small contraction in growth in Q2, after the recovery in GDP over the prior six months. The soft domestic activity backdrop contributed to slightly lower NZGB and swap rates, against the global trend, leading to lower NZ-global rate spreads across the board.

The theme for currency markets was a broad-based bounce-back in the USD. After falling for six consecutive months (down 10.4% over the first half of the year), the USD DXY index rose 3.3% in July. This could have reflected some closing of short USD positions that had accrued, supported by the backdrop of positive US economic data surprises and reduced conviction that the Fed was about to restart the easing cycle.

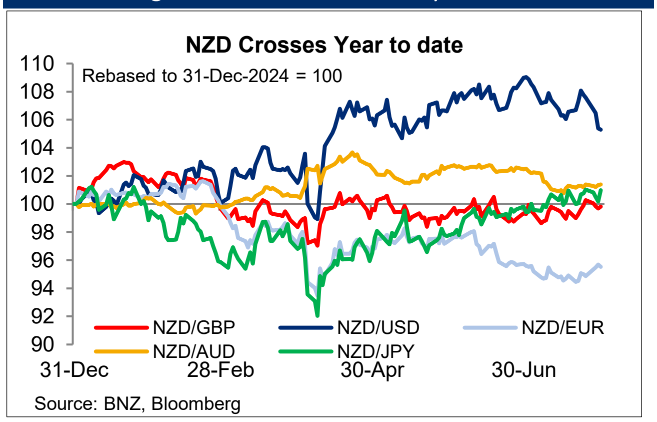
NZ core CPI inflation measures settle around 2.3-2.8%



NZ GDP looks to have contracted



NZD flat to higher on most crosses this year



NZD/USD fell 3.4% for the month to 0.5890. It traded from a high of 0.6120 on the first day of the month to a low of 0.5888 on the last day of the month in the wake of the Fed's policy update. While NZD/USD was weaker through the month, the bigger picture was one of the NZD maintaining the range-trading environment exhibited since the second half of April.

NZD cross movements were small by comparison, with modest net movements. NZD/AUD fell 1% to 0.9165, driven by lower NZ-Australia rate spreads. Early in the month, the RBA shocked the market, keeping policy steady against high expectations of a 25bps cut. Governor Bullock emphasised that the decision to hold was about timing rather than direction. Data during the month cemented in views that the RBA would cut at the August meeting, with a surprising two-tenths lift in the unemployment rate to 4.3%. Australian Q2 CPI data were on the softer side of expectations, with the key trimmed mean measure of core inflation running at 0.6% q/q, resulting in the annual figure falling two-tenths to a 3½-year low of 2.7%, close to the mid-point of the RBA's 2-3% target range.

The European Central Bank didn't surprise, leaving rates unchanged at 2.0%. President Lagarde repeated the line about not pre-committing to a particular rate path and the bank would continue to follow a data-dependent and meeting-by-meeting approach. Euro area GDP rose 0.1% in Q2, with small contractions in Germany and Italy, offset by growth for France and Spain. The tepid lift in activity followed the solid 0.6% gain in Q1. NZD/EUR traded a range of not much more than 1 cent for the month, between 0.5080-0.5190.

NZD/GBP also traded a narrow range of 0.44-0.4490. UK economic data pointed to weak growth in Q2 after the surprising strength in Q1, while the UK unemployment rate rose to a four-year high of 4.7%. Alongside signs of moderating wage inflation, the data reinforced expectations of a BoE rate cut in August.

NZD/JPY traded a tight range, with some upward drift, reaching a six-month high of just over 89 towards the end of the month. The result of Japan's Upper House election was the ruling LDP/Komeito coalition losing its majority. The outcome will result in months of political uncertainty, and the fate of PM Ishiba hangs in the balance. The market took the view that political uncertainty would likely keep the BoJ on the sidelines for a while longer against the backdrop of inflation remaining high. The BoJ left policy unchanged and Governor Ueda's comments were on the dovish side, as didn't offer much in the way of providing guidance that tighter policy was imminent.

China GDP data released for Q2 were solid, with growth continuing to run ahead of its annual 5% growth target. Less encouraging, there were continued signs of a two-speed economy, with strong exports against a backdrop of sluggish domestic demand (not helped by the deep downturn in the property sector), evident in the trade surplus pushing up to a fresh high of 6% of GDP. With a tightly managed exchange rate, USD/CNY showed only a modest increase, so NZD/CNY fell nearly 3%.

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Monthly Performance Table

	end-Jul	end-Jun	Change
Currencies			
NZD/USD	0.5890	0.6098	-3.4%
NZD/AUD	0.9166	0.9265	-1.1%
NZD/EUR	0.5159	0.5173	-0.3%
NZD/GBP	0.4460	0.4440	0.5%
NZD/JPY	88.79	87.80	1.1%
NZD/CNY	4.245	4.366	-2.8%
TWI	68.6	69.9	-1.7%
AUD/USD	0.6426	0.6582	-2.4%
EUR/USD	1.1415	1.1787	-3.2%
GBP/USD	1.3207	1.3734	-3.8%
USD/JPY	150.77	144.02	4.7%
USD/CNY	7.20	7.16	0.5%
USD/CAD	1.3855	1.3608	1.8%
USD DXY	100.03	96.88	3.3%
Asia dollar index	91.73	93.04	-1.4%
Equity Markets			
MSCI AC Wrld, loc.	2,617	2,561	2.2%
MSCI World, loc.	14,998	14,697	2.0%
MSCI EM, USD		3,298	~2.5%
US S&P 500	6,339	6,205	2.2%
Euro STOXX 600	546.1	541.4	0.9%
Germany DAX	24,065	23,910	0.7%
France CAC 40	7,772	7,666	1.4%
UK FTSE 100	9,133	8,761	4.2%
Aust S&P/ASX 200	8,743	8,542	2.3%
Japan Topix	2,943	2,853	3.2%
China CSI 300	4,076	3,936	3.5%
NZX50	12,824	12,603	1.8%
Volatility: VIX	16.72	16.73	-0.1%
3-mth Money Market Futures			
NZD Dec-25	96.95	96.93	0.02
AUD Dec-25	96.72	96.92	-0.20
USD Dec-25	95.97	96.33	-0.36
EUR Dec-25	98.08	98.20	-0.12
GBP Dec-25	96.29	96.39	-0.10
CAD Dec-25	97.41	97.62	-0.22

	end-Jul	end-Jun	Change
NZ Rates			
OCR	3.25	3.25	0.00
NZ 90day BB	3.20	3.29	-0.10
NZ 2yr swap	3.16	3.19	-0.03
NZ 5yr swap	3.54	3.57	-0.02
NZ 10yr swap	4.05	4.08	-0.03
NZ Govt (4/27)	3.25	3.31	-0.06
NZ Govt (5/30)	3.82	3.86	-0.05
NZ Govt (5/35)	4.51	4.54	-0.02
NZ Govt (5/41)	5.00	4.97	0.03
Global 10 year bond rates			
US	4.38	4.23	0.15
Canada	3.46	3.27	0.18
UK	4.57	4.49	0.08
France	3.35	3.28	0.06
Germany	2.69	2.61	0.09
Italy	3.51	3.48	0.03
Spain	3.27	3.24	0.03
Portugal	3.12	3.05	0.06
Ireland	2.91	2.92	0.00
Japan	1.55	1.43	0.12
Australia	4.26	4.16	0.10
Commodities (USD)			
WTI Crude	69.26	65.11	6.4%
Brent Crude	72.53	67.61	7.3%
R/B CRB Index	299.8	297.3	0.8%
Gold spot	3,290	3,303	-0.4%
Silver spot	36.71	36.11	1.7%
Copper	435.5	503.0	-13.4%
Iron Ore	99.76	93.75	6.4%
Thermal coal	115.15	109.90	4.8%
Corn	413.8	425.5	-2.8%
Wheat	523.3	538.3	-2.8%
SGX-NZX Dairy WMP	3,945	3,755	5.1%
SGX-NZX Milk Price '26	10.10	9.75	3.6%

Source: BNZ, Bloomberg

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